No. 10,455

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

WESTERN VEGETABLE OILS COMPANY, INCORPORATED (a corporation),
Appellant,

vs.

SOUTHERN COTTON OIL COMPANY (a corporation), SOUTHERN PACIFIC COMPANY (a corporation),
Appellees.

BRIEF FOR APPELLANT.

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I.

JURISDICTIONAL STATEMENT.

Western Vegetable Oils Company, Incorporated, defendant below, appeals from an order of the United States District Court for the Northern District of California, Southern Division, denying the motion of appellant to stay proceedings in the District Court pending arbitration. (Tr. p. 29.)

The action was brought in the District Court by Southern Cotton Oil Company, a corporation organized and existing under the laws of New Jersey, as plaintiff, against Southern Pacific Company, a corpo-

ration organized and existing under and by virtue of the laws of Kentucky, and Western Vegetable Oils Company, Incorporated, a corporation organized and existing under and by virtue of the laws of the State of California, as defendants.

The complaint (Tr. p. 2) sets forth a cause of action for damages resulting from the loss in transit of a tank car of coconut oil purchased by plaintiff, Southern Cotton Oil Company, from defendant, Western Vegetable Oils Company, Incorporated and transported by defendant, Southern Pacific Company. The damages sought are $3847.50, exclusive of interest and costs.

The answer of defendant, Western Vegetable Oils Company, Incorporated (Tr. p. 15) pleads as a defense to the action a contract under which the tank car of coconut oil was purchased, alleging that by the terms of said contract the dispute, which is the subject of the action so commenced by Southern Cotton Oil Company, must be submitted to arbitration.

Subsequently, and before the action was set for trial, Western Vegetable Oils Company, Incorporated filed its motion to stay proceedings in the action until arbitration under the terms of the contract could be had. (Tr. p. 23.)

(a) The District Court has jurisdiction of the parties and the subject matter of the action by virtue of Section 41, 28 U.S.C.A.

(b) This Court has jurisdiction upon appeal to review the said order of the District Court denying

the motion of Western Vegetable Oils Company, Incorporated, to stay the action under and by virtue of Section 227, 28 U.S.C.A.

(c) The pleadings which show the existence of the jurisdiction are the complaint (Tr. p. 3), the answer of defendant, Western Vegetable Oils Company, Incorporated (Tr. p. 15), and the motion of defendant, Western Vegetable Oils Company, Incorporated, to stay proceedings. (Tr. p. 23.)

II.

STATEMENT OF THE CASE.

On the 18th of June, 1941, Western Vegetable Oils Company, Incorporated, and Southern Cotton Oil Company entered into a contract (Tr. p. 20) under which Western Vegetable Oils Company, Incorporated agreed to sell to Southern Cotton Oil Company five tank cars, approximately 60,000 pounds each, of crude coconut oil. The contract specified that shipment was to be made in July, 1941 in "Seller's Tankcars" and the price was specified to be "Five and Seven Eighths Cent (5⅞¢) per pound, F.O.B. Seller's Plant, Outer Harbor, Oakland, California".

This contract also contained as its final paragraph a clause reading as follows:

> "(6) This contract shall be deemed to be made and performed in California and is to be governed by the laws thereof,
>
> Clause Paramount: This contract is subject to the published Rules and Regulations of the Na-

> tional Institute of Oilseed Products—and which are hereby made a part of this contract, except insofar as such Rules and Regulations are modified or abrogated by this contract." (Tr. p. 22.)

The published rules and regulations of the National Institute of Oilseed Products (Tr. p. 37), referred to in paragraph (6) of the contract quoted above contained, among other rules, the following:

> "Rule 64.—Any dispute arising under contracts which cannot be settled amicably between interested parties shall immediately be submitted to arbitration before a committee selected by the San Francisco Chamber of Commerce under the Rules of the National Institute of Oilseed Products." (Tr. p. 54.)

On July 18, 1941 one tank car of coconut oil was shipped by appellant Western Vegetable Oils Company, Incorporated from Oakland, California under this contract. Shipment was made by delivery of this tank car to defendant and appellee Southern Pacific Company, as alleged in paragraph VII of the complaint of Southern Cotton Oil Company. (Tr. p. 4.) Plaintiff and appellee Southern Cotton Oil Company alleges in its complaint that the shipment of coconut oil was lost in transit, which defendant and appellee Southern Pacific Company admits in its answer.

Subsequent to the loss of the contents of this tank car of coconut oil correspondence ensued between appellant and Southern Cotton Oil Company with respect to responsibility for the loss. This correspondence is set forth in exhibits to the affidavit of Adolph

Schumann in support of appellant's motion to stay proceedings in this action. (Tr. p. 26.) As shown by Exhibit "A" to this affidavit (Tr. pp. 29-30), appellant proposed arbitration of the dispute. As shown by Exhibit "A" to Mr. Schumann's affidavit (Tr. pp. 32-33), appellee Southern Cotton Oil Company responded to this propsal as follows:

> "Mr. Schumann refers to arbitration, and it seems to me that if there is any arbitration, it should be between the Western Vegetable Oils Company and the railroad, because we should not be made to stand any part of the loss."

Subsequently and on November 19, 1942 the complaint was filed in the District Court.

On January 12, 1943 defendant and appellant Western Vegetable Oils Company, Incorporated filed its answer in the action in the District Court setting forth the contract between appellant and appellee Southern Cotton Oil Company dated the 18th day of June, 1941 (Tr. p. 20), setting forth rule 64 of the published rules and regulations of the National Institute of Oilseed Products and asking for a stay of proceedings until arbitration under these rules could be had.

On February 3, 1943 appellant Western Vegetable Oils Company, Incorporated filed its motion to stay the action in the District Court until such arbitration could be had. (Tr. p. 23.) After hearing, the District Court filed on April 2, 1943 its memorandum and order denying motion to stay trial. (Tr. p. 90.)

III.

SPECIFICATIONS OF ERROR.

(1) The District Court erred in holding that the controversy which is the subject matter of this action does not come within the arbitration clause of the contract between plaintiff and appellee, Southern Cotton Oil Company, and defendant and appellant, Western Vegetable Oils Company, Incorporated.

(2) The District Court erred in denying the motion of defendant and appellant Western Vegetable Oils Company, Incorporated to stay proceedings in the action before the District Court until arbitration of the controversy could be had.

IV.

STATEMENT OF THE ARGUMENT.

The controversy which is the subject matter of the action in the District Court arises under a written contract, containing a provision to settle by arbitration a controversy thereafter arising out of the contract. As set forth in the statement of the case the contract (Tr. p. 22) contains the following provision:

> "Clause Paramount: This contract is subject to the published Rules and Regulations of the National Institute of Oilseed Products—*and which are hereby made a part of this contract,* except insofar as such Rules and Regulations are modified or abrogated by this contract." (Emphasis supplied.)

It thus appears that by the terms of the clause paramount the rules and regulations of the National Institute of Oilseed Products were incorporated by reference in the contract between the parties. It is well established that such a reference in a contract to another document renders the other document a part of the contract. As also set forth in the statement of facts, the published rules and regulations of the National Institute of Oilseed Products contain the following rule:

> "Rule 64.—Any dispute arising under contracts which cannot be settled amicably between interested parties shall immediately be submitted to arbitration before a committee selected by the San Francisco Chamber of Commerce under the Rules of the National Institute of Oilseed Products."

This rule is therefore made a provision of the contract requiring controversies arising under the contract to be settled by arbitration. A similar situation, involving the incorporation of a provision for arbitration in a contract by reference in the contract to another document is presented by *Hines v. Ziegfeld,* 226 N. Y. Supp. 562 (1928). In this case an agreement to employ an actress provided that all of the terms and conditions of the actor's equity form of contract should be deemed to be a part of the agreement. The actor's equity form of contract contained a clause providing for the arbitration of any dispute arising under the contract. The court held that the terms of the actor's equity form of contract, includ-

ing the provision requiring arbitration of disputes arising under the contract, were a part of the agreement between the parties and had been incorporated by reference in it. The court said, in 226 N. Y. Supp. at p. 566:

> "Here it is expressly provided that certain provisions for arbitration shall be made a part of the contract between the parties. The arbitration clause therefore is applicable, and it follows that all questions for decision must be decided by arbitration."

In reaching its decision in *Hines v. Ziegfeld,* supra, the court specifically distinguished cases in which an arbitration clause contained in a separate document, but not stated to be made a part of the agreement out of which the dispute arose, had been held not to be a part of the agreement. There can be no question, in view of the language used in the "Clause Paramount" that the parties intended that the rules of the National Institute of Oilseed Products, and all of them, were specifically to be considered a part of their contract of sale.

In *Marine Transit Corporation v. Dreyfus,* 284 U.S. 263, 52 S. Ct. 156, 76 L. Ed. 282, the parties had entered into a contract called a "booking agreement" under which Marine Transit Corporation agreed to furnish to Louis Dreyfus & Company canal tonnage for the transportation of wheat. The contract between the parties provided that it should be "subject to the New York Produce Exchange Canal Grain Charter Party No. 1 as amended." The charter party

contained a provision requiring arbitration of all disputes arising under it. The charter party was a separate document referred to in the contract between the parties. The contract does not appear to have stated specifically that the charter party was deemed to be a part of the contract. A shipment of wheat carried in a barge furnished under the contract was lost and Louis Dreyfus & Co. filed a libel in admiralty to recover damages for loss of the wheat and later moved for a reference of the dispute to arbitration. The court held that the dispute was referable to arbitration under the contract and, in doing so, necessarily held that the provision for arbitration contained in the charter party was a part of the contract to furnish tonnage. The court said in 76 L. Ed. at p. 286:

> "There is no question that the controversy between the petitioner and the respondents was within the arbitration clause of the booking contract."

It is noteworthy that in several cases arising in California the provisions of a separate document, not stated in the agreement as having been made a part of the agreement, have been held to have become a part of the agreement by much less explicit reference. In *Asnon v. Foley,* 105 Cal. App. 624 (1930), the contract provided that:

> "Labor and materials furnished to be governed by Pacific Coast Sales Book plus ten per cent."

The Pacific Coast Sales Book was used by contractors and showed prices of construction materials as

they varied from time to time. The court held that the prices so specified were the prices applicable to the contract between the parties.

In *Bell v. Rio Grande Oil Company,* 23 Cal. App. (2d) 436 (1937), an agreement to make a lease embodied in a letter written and signed by the parties stated:

> "Your lease to us is to be Oil Age Form 86, with modification to conform with this letter."

The Oil Age Form 86 contained, as one of its standard provisions, a surrender clause, permitting the lessee to quitclaim the leasehold to the lessor upon payment of a certain sum as liquidated damages, upon which all rights and obligations of the parties would terminate. Subsequently the lessee surrendered the lease and the lessor attempted to treat the surrender as a breach of the original agreement to lease the property.

The court held that the surrender clause contained in Oil Age Form 86 was a part of the agreement between the parties, saying in 23 Cal. App. (2d) at p. 440:

> "A written agreement may, by reference expressly made thereto, incorporate other written agreements; and in the event such incorporation is made, the original agreement and those referred to must be considered and construed as one."

Again in *Beedy v. San Mateo Hotel Company,* 27 Cal. App. 653 (1915), an agreement to subscribe to

shares of stock referred to "the annexed 'List of subscribers to capital stock in the San Mateo Hotel project' ". The court held that the subscription agreement and the list of subscribers constituted one document even though the list of subscribers appeared not to have been actually "annexed" to the subscription agreement, and further held that actual annexation was not essential to a merger by reference of the separately executed documents.

It thus appears that the rules of the National Institute of Oilseed Products would have become a part of the agreement between appellant and appellee, Southern Cotton Oil Company, even without the specific statement in the agreement that the rules "are hereby made a part of this contract". However, the use of this language places the matter beyond question.

In these circumstances the agreement to submit to arbitration controversies arising under the contract is valid, irrevocable and enforceable within the meaning and intent of the laws of the United States and of the State of California. The provisions of the United States Arbitration Act, Title 9, Sections 1 to 15, U.S.C.A. and of the Code of Civil Procedure of the State of California, Title X, Sections 1280 to 1293 are closely similar.

The United States Arbitration Act, Title 9, Section 2, U.S.C.A., provides as follows:

> "A written provision in any maritime transaction or a contract evidencing a transaction in-

volving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."

Section 1280 of the Code of Civil Procedure of the State of California provides as follows:

"Validity of arbitration agreements. A provision in a written contract to settle by arbitration a controversy thereafter arising out of the contract or the refusal to perform the whole or any part thereof, or an agreement in writing to submit an existing controversy to arbitration pursuant to section 1281 of this code, shall be valid, enforceable and irrevocable, save upon such grounds as exist at law or in equity for the revocation of any contract; provided, however, the provisions of this title shall not apply to contracts pertaining to labor."

Both of the foregoing statutory provisions are applicable to this case. The contract between appellant and appellee, Southern Cotton Oil Company, provides in its final paragraph, as stated in the statement of facts, a clause reading as follows:

"(6) This contract shall be deemed to be made and performed in California and is to be governed by the laws thereof."

It is thus the expressed intention of the parties that the laws of California should govern their rights and obligations under the contract.

Furthermore, since the contract between these parties plainly evidences "a transaction involving commerce", in that it involves sales made in interstate commerce and since the plaintiff and appellee, Southern Cotton Oil Company, chose to bring an action upon the contract in a court of the United States, the provisions of the United States Arbitration Act are equally applicable.

The validity of both statutes, Federal and State, is no longer open to any question. In *Marine Transit Corporation v. Dreyfus,* supra, the Supreme Court of the United States considered the United States Arbitration Act, held it constitutional, and sustained the action of the District Court in issuing its order compelling the parties to arbitrate the controversy involved in this action. This controversy involved the right of Louis Dreyfus & Company to recover damages for the loss of a cargo of wheat carried in a barge provided by Marine Transit Corporation pursuant to the contract.

More recently in *Kulukundis Shipping Co. v. Amtorg Trading Corporation,* 126 Fed. (2d) 978, the court considered the United States Arbitration Act and its history at length, holding that an agreement to arbitrate disputes contained in a charter party was binding upon the parties and required submission to arbitration of a claim for damages for breach of contract.

In *Parry v. Bache,* 125 Fed. (2d) 493, the court held that a dispute arising under a written contract providing for the arbitration of such disputes was enforceable and that a stay of proceedings should be granted by the federal court in which action upon the contract was brought even though under the law of Florida, where the contract was made, the agreement of arbitration may not have been enforceable.

The validity of the California statutes above cited has been upheld in several cases. In *Snyder v. The Superior Court,* 24 Cal. App. (2d) 263, the constitutionality of Title X of the Code of Civil Procedure of the State of California was specifically upheld by the Supreme Court of the State of California. The same result was reached in *Pacific Indemnity Co. v. Insurance Co. of North America,* 25 Fed. (2d) 930, in which the arbitration statutes of the State of California were in issue and in which the claim of unconstitutionality had been made.

It is equally certain that the controversy which is the subject matter of the action in the District Court is a controversy which is referable to arbitration under the terms of the contract and is required by the terms of the contract to be submitted to arbitration. The complaint of plaintiff and appellee, Southern Cotton Oil Company, alleges in paragraph IX (Tr. p. 5) that the defendant and appellant, Western Vegetable Oils Company, Incorporated and the defendant and appellee, Southern Pacific Company failed and neglected to deliver the shipment of coconut oil to

the plaintiff and appellee at Gretna, Louisiana. In paragraph XI of the complaint (Tr. p. 6) the plaintiff and appellee alleges various acts of negligence on the part of both defendants in providing a proper tank car in which to make shipment and in properly loading and inspecting the car. In paragraph XII of the complaint (Tr. p. 6) the plaintiff alleges that it has been damaged "by reason of the premises".

The District Court appears in its opinion (Tr. p. 92) to have construed the complaint as setting forth only a claim for damages for negligent conduct causing the loss of the shipment saying (Tr. p. 92): "The question to be determined is whether there is negligence of the seller or of the shipper or of both which caused the loss." The District Court then concludes that the dispute is outside of, rather than within, the contract.

The District Court overlooks the fact that the allegations of paragraph IX of the complaint would support a judgment for damages for breach of contract, irrespective of negligence. However, disregarding for the purposes of discussion the allegations of paragraph IX of the complaint, the District Court fails to recognize that all of the allegations of negligence on the part of the appellant contained in paragraph XI of the complaint constitute allegations of negligence in the performance of duties required by the contract to be performed. These allegations are of course denied by the appellant in paragraph III of its answer. (Tr. p. 17.)

It must be observed that the contract specifies "Packing: Seller's Tankcars" and by its terms contemplated shipment from "Seller's Plant, Outer Harbor, Oakland, California." (Tr. p. 21.)

There is thus imposed upon appellant as seller, by the contract itself, the duty to furnish a suitable tank car in proper condition, and to load and inspect the car in such a manner as to guard against loss of the contents. These duties are created by the contract, which created the relationship between the seller and the buyer of the oil out of which this entire controversy grows. Thus, in settling this controversy and in determining questions of negligence, it is necessary to decide how far the seller performed, or failed to perform, the duties imposed upon it by the contract. This is clearly a controversy arising under the terms of the contract, since it is the contract itself which gives rise to the duties of the seller. It is elementary that there is no responsibility for negligent conduct unless there is a corresponding duty arising from some source to exercise due care. The source from which any duties of appellant to appellee Southern Cotton Oil Company arise is the contract between them.

An arbitration agreement of this type is broad enough to cover any such controversy as is here involved. General arbitration agreements have been held to cover a wide variety of disputes beeween the parties to the agreement. In *Shanferoke Coal and Supply Corp. v. Westchester Service Corp.,* 70 Fed. (2d) 297, the dispute arose under a contract for the sale of a quantity of coal over a period of years. The plaintiff

claimed as damages the commissions upon the quantity of coal which the defendant refused to purchase from the plaintiff. The court said in 70 Fed. (2d) at p. 299:

> "* * * a clause of general arbitration does not cease to be within the statute when the dispute narrows down to damages alone. General Footwear Co. v. A. C. Lawrence Leather Co., 252 N. Y. 577, 170 N. E. 149; Merchant v. Mead-Morrison Co., 252 N. Y. 284, 298, 299, 169 N. E. 386. If the clause is general in form, it makes no difference what may come up under it."

In *In re Utility Oil Corporation,* 69 Fed. (2d) 524, a charter party contained a general arbitration clause stating that:

> "Any dispute arising during performance of this Charter Party shall be settled by arbitration in New York, * * *"

A claim was made for damages for breach of the charter, arising from the refusal of the charterer to deliver any further cargoes to the vessel. The court said in 69 Fed. (2d) at p. 526:

> "A dispute arose under the contract, for here one of the parties, in the opinion of the other, failed to perform. Arbitration clauses are designed to provide remedies for such situations. * * * But it is argued that the appellant terminated performance and therefore the arbitration clause does not apply. The parties clearly intended to arbitrate 'any dispute arising during the performance of this Charter Party'. Their intention so to do should be strictly observed."

In *Kulukundis Shipping Co. v. Amtorg Trading Corporation,* supra, the dispute to be arbitrated again involved damages for breach of contract arising through failure of one of the parties to perform a charter party. The court said in 126 Fed. at p. 988:

> "The arbitration clause here was clearly broad enough to cover the issue of damages; * * *"

The court further cited with approval the language quoted above from *Shanferoke Coal and Supply Corp. v. Westchester Service Corp.,* supra.

It is to be noted also that the same broad construction has been placed upon general arbitration clauses by the courts of the State of New York, which enacted one of the first general arbitration statutes. In *Berkovitz v. Arbib,* 183 New York Supp. 305 (1920), a contract for the purchase of skins contained the following clause:

> "Skins to be the usual quality of their kind, and claims in regard thereto shall not invalidate this contract, but shall be settled amicably or by arbitration in New York in the usual manner."

The purchaser refused to pay for the skins on the ground that quantities and weights were not in accordance with the contract, and resisted arbitration on the ground that by virtue of the clause above quoted arbitration was to apply only to questions of "quality". The Court held that the contract provided for arbitration no matter what the ground for failure to perform the contract may have been.

In *General Footwear Corporation v. Lawrence Leather Company,* 252 New York 577, 170 N. E. 149, the parties had entered into a contract by which the defendant was to sell to the plaintiff a quantity of lamb skins. The contract contained a clause as follows:

> "Arbitration. Any dispute arising under this contract shall be submitted to an arbitrator to be agreed upon by the parties."

Plaintiff brought an action to compel the parties to proceed to arbitration, claiming damages for breach of contract arising from the defendant's failure to deliver the skins. The defendant asserted that such a breach was not a matter for arbitration under the contract. The court held that the language of the arbitration provision was broad enough to cover any dispute arising under the contract and compelled arbitration.

In *Freydberg Bros. v. Corey,* 31 New York Supp. (2d Series) 10 (1941), the provision for arbitration read as follows:

> "Any dispute of any nature that might arise between us is to be adjusted by the American Arbitration Association."

The dispute between the parties was as to whether the arbitrator himself could determine whether or not he possessed jurisdiction of a given dispute. The court said, at page 11:

> "This language would seem to authorize the arbitrator to pass upon any dispute whatsoever arising out of the employment relationship between the parties."

Since, as pointed out above, even the most narrow construction of the complaint in this action involves the question as to whether the appellant properly performed duties imposed upon it by the contract, there can be no doubt that the arbitration clause is broad enough to cover the dispute.

In the circumstances of this case the power, and indeed the duty, of the District Court to stay the action before it until arbitration can be had is not to be doubted. Section 3 of the United States Arbitration Act reads as follows:

> "If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration."

Section 1284 of the Code of Civil Procedure reads as follows:

> "Stay of civil action. If any suit or proceeding be brought upon any issue arising out of an agreement providing for the arbitration thereof, the court in which such suit or proceeding is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration, shall stay the action until an arbitration has been had in accordance with the terms of the

agreement; provided, that the applicant for the stay is not in default in proceeding with such arbitration."

Defendant and appellant, Western Vegetable Oils Company, Incorporated, set forth in its answer (Tr. p. 15) the existence of the contract between it and plaintiff and appellee, Southern Cotton Oil Company, and the provisions of the contract requiring arbitration. In its prayer for relief (Tr. p. 19) appellant requested that the action be stayed until the required arbitration could be had. Subsequently, and before the action could be set for trial, appellant filed its notice of motion to stay the action upon the same grounds. (Tr. p. 23.) It must further be observed that appellant filed in the action the affidavit of Adolph Schumann (Tr. p. 26), the president of appellant, Western Vegetable Oils Company, Incorporated, to which affidavit were attached various exhibits referred to in the statement of the case showing that he as president of appellant proposed arbitration long before this action was commenced.

In these circumstances it is submitted that the case of *Shanferoke Coal & Supply Corp. v. Westchester Corp.,* supra, later affirmed by the Supreme Court of the United States in 293 U. S. 449, 79 Law. Ed. 583, is decisive, not only of the question of the power of the District Court to grant the stay of proceedings, but also upon the question of any alleged default of appellant in seeking arbitration. In this case the contract between the plaintiff and defendant involved the sale of coal upon commission. The de-

fendant repudiated the contract after two-thirds of the quantity of coal remained to be delivered and the plaintiff brought suit for commissions which would have been earned. The contract contained a provision requiring that "In case any dispute should arise between the Buyer and the Seller as to the Performance of any of the terms of this agreement" such dispute should be submitted to arbitration, and further providing that if the arbitration should fail to proceed to a final award, "either party may apply to the Supreme Court of the State of New York for an order compelling the specific performance of this arbitration agreement in accordance with the arbitration laws of the State of New York".

It further appears that the defendant, upon suit being filed, filed its answer setting up the contract requiring arbitration as a defense, and seeking a stay of proceedings.

On these facts, strikingly similar to the instant case, both the Circuit Court of Appeals and the Supreme Court held that the District Court in which the action was brought had power to stay the action under the provisions of the United States Arbitration Act. It is particularly significant that both courts stated that this power existed even though, by virtue of the reference in the contract to the laws of New York the District Court might not have had power specifically to compel arbitration of the controversy, i.e., that even though this latter power was by contract conferred only upon a state court, the power to stay the action existed in the federal court.

In this case also there is the striking similarity with the instant case that defendant was alleged to be in default in proceeding with the arbitration because it raised the question of arbitration for the first time in its answer. Both courts squarely held that, having raised the defense in the answer, the defendant was not in default. In the instant case, an inspection of the affidavit of the president of appellant will show that appellant requested arbitration long prior to the commencement of any action, so that there is even less merit for the contention that appellant is in default. In this connection it is worth mentioning that we have been able to find no case in which a party desiring arbitration is held to have been in default when he raises the question of arbitration in his answer to a suit upon the agreement. Of course, where the defendant does not raise his defense in his answer, but pleads to the merits of the action and seeks affirmative relief without regard to the arbitration clause of his contract the defendant has been held, as in *Radiator Speciality Co. v. Cannon Mills,* 27 Fed. (2d) 318, to have waived the defense.

The facts in the instant case are altogether different. As to both the questions of the power of the District Court to grant the stay sought and as to the defendant being in default in seeking arbitration it would be possible to quote virtually the whole of the opinions in the *Shanferoke* case, but it is deemed unnecessary to do so. On the question of default, however, one quotation may well be emphasized. The court says in 70 Fed. (2d) at page 299:

> "The plaintiff further objects that the defendant is 'in default in proceeding with such arbitration,' within the meaning of section 3. True, it has not named its arbitrator, but in its answer and moving affidavits has merely expressed its willingness to submit to arbitration. This appears to us enough. It was the plaintiff who declared the contract to be at an end; and with that the defendant was contented. If the plaintiff meant to proceed further and enforce a claim for damages, the initiative rested upon it; it should have named the first arbitrator. If it did not but sued instead, it was itself the party who fell 'in default in proceeding with such arbitration,' not the defendant."

A very similar result was reached in *Kulukundis Shipping Co. v. Amtorg Trading Corporation,* supra. There the appellant originally filed an answer to the complaint without referring to the arbitration provisions of the contract. Nine months later, and two months before the trial, the appellant sought to amend its answer to allege the arbitration agreement as a defense to the action. The Circuit Court of Appeals held that the amendment should have been allowed and that the District Court should have stayed the action pending arbitration. This case again illustrates both the power and the duty which rests upon the District Court to stay proceedings in the action when such a stay is requested. It also shows most strongly that so long as the defense of the agreement to arbitrate is raised by answer the defendant cannot be held to be in default in proceeding with the arbitration.

In the case at bar there can be no question that the defendant and appellant is not in such default.

Parry v. Bache, supra, presents an example of the granting of the stay of proceedings in a federal court where no right to such a stay would have existed under state law. There the suit was originally brought in the state court of Florida and removed to the federal court. It was claimed that the Florida law did not recognize the enforceability of the arbitration agreement. The court held that the United States Arbitration Act controlled the procedure in the federal court and that the view that the state court might have taken of the agreement was immaterial.

In the instant case the law of the State of California, upon which the parties in their contract agreed to be bound, and the federal law as well, require the granting of the stay of proceedings in the circumstances here presented.

The District Court appears to have thought that the stay of proceedings should not be granted because of the presence of Southern Pacific Company as a defendant in the action. Neither the United States Arbitration Act nor the statutes of the State of California above cited authorize the court to refuse to grant the stay of proceedings on any such ground. The stay of proceedings is authorized by the statutes because the parties to the dispute have bound themselves by their contract to arbitrate the dispute. The fact that someone not a party to the contract is involved in the dispute to be arbitrated can have no bearing upon the validity of the agreement to arbitrate and

cannot prejudice the right to arbitration to which the party seeking it is entitled. So long as the conditions of section 3 of the United States Arbitration Act and section 1284 of the Code of Civil Procedure of the State of California are met it is the duty of the court to grant the stay. It is not one of the conditions of these statutes that no other parties should be involved in the litigation. It is obvious that a very large proportion of disputes arising under a contract providing for arbitration could involve in one way or another persons who were not parties to the arbitration agreement, and to refuse to grant the stay in all such circumstances would deprive the statutes authorizing the stay of the greater part of their meaning.

When the issue between the parties to the arbitration agreement has been determined by arbitration such further proceedings may be taken in the action as may be necessary to determine the rights and duties of the parties to the action who were not parties to the agreement of arbitration. In fact, *Marine Transit Corporation v. Dreyfus,* supra, shows that it is proper to refer to arbitration under such an agreement the portion of the dispute between the parties which is subject to the arbitration agreement. There the claim *in personam* against Marine Transit Corporation and not the claim *in rem* against one of the vessels involved in the loss of the cargo was referred to arbitration although both claims were involved in the original action.

It should be noted that the appealability of the order of the District Court denying the appellant's motion

to stay proceedings is established by *Shanferoke Coal and Supply Corp. v. Westchester Service Corp.*, supra, in which the Supreme Court holds that the motion for stay of proceedings is in the nature of an application for an interlocutory injunction, that the District Court's order upon the motion is an interlocutory order, and is therefore appealable to the Circuit Court of Appeals under section 129 of the Judicial Code, Title 28, section 227, U.S.C.A.

It is respectfully submitted that for the reasons set forth herein the order of the District Court should be reversed with directions to the District Court to grant a stay of proceedings in this action until arbitration can be had.

Dated, San Francisco,
July 28, 1943.

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